No. 79-278

In the Supreme Court of the United States

OCTOBER TERM, 1978

LAWRENCE CONNELL, CHAIRMAN OF THE NATIONAL CREDIT UNION ADMINISTRATION BOARD, ET AL., *Petitioners*

v.

AMERICAN BANKERS ASSOCIATION, ET AL.

FEDERAL HOME LOAN BANK BOARD, ET AL., *Petitioners*

v.

INDEPENDENT BANKERS ASSOCIATION OF AMERICA

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM, ET AL., *Petitioners*

v.

UNITED STATES LEAGUE OF SAVINGS ASSOCIATIONS

In Support of Petition For a Writ of Certiorari To the United States Court of Appeals For The District of Columbia Circuit

BRIEF OF CREDIT UNION NATIONAL ASSOCIATION, INC. AND NATIONAL ASSOCIATION OF FEDERAL CREDIT UNIONS, INC., AMICI CURIAE

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Credit Union National Association, Inc. and the National Association of Federal Credit Unions, as *amici curiae,* submit this Brief in support of the Petition for Certiorari of the Solicitor General on behalf of the National Credit Union Administration and its

Chairman Lawrence Connell for review of the judgment of the U.S. Court of Appeals in *Connell* v. *American Bankers Assoc.*

INTEREST OF THE AMICI

Credit Union National Association, Inc. (CUNA) and the National Association of Federal Credit Unions, Inc. (NAFCU) are credit union associations whose members and affiliates include nearly all federal credit unions operating share draft programs that are the subject of this case.

CUNA represents the interests of 8,202 state and 11,841 federal credit unions that are affiliated with CUNA through membership in 51 state and area credit union leagues. The membership of NAFCU consists of 401 federal credit unions, whose assets account for more than one-third of the total assets of all federal credit unions.

CUNA and NAFCU jointly participated in this matter as *amici curiae* in the District Court and before the Court of Appeals. Pursuant to Rule 42(1) of this Court, CUNA and NAFCU have received consent to file this Brief from all of the parties to this case and the two companion cases, *Federal Home Loan Bank Board* v. *Independent Bankers* and *Board of Governors* v. *U.S. League of Savings Assoc.*

ARGUMENT

a. Introductory Statement

On April 20, 1979, the U.S. Court of Appeals for the District of Columbia entered its judgment in *American Bankers Assoc.* v. *Connell* and, reversing the District Court, held that the petitioner National Credit Union Administration (NCUA) had violated the statutes it administers by issuing regulations for the withdrawal of accounts in federal credit unions by means of negotiable or transferable share drafts. (12 C.F.R. 701.34.). In the same decision, the Court of Appeals decided two companion cases and held that bank automatic transfer services and federal savings and loan remote service units had also been established in violation of federal law.

If the decision of the Circuit Court is allowed to take effect on January 1, 1980, as now ordered, the impact on the nation's credit unions and their members will be enormous. Directly affected will be the more than one million Americans already relying on share drafts to conduct their daily financial affairs. Additionally affected will be the millions more who belong to federal credit unions that will be unable to commence share draft programs if the decision of the Court becomes final.

Of even broader concern than the issue of share drafts themselves, the Court of Appeals' decision has thrown into complete uncertainty the whole meaning of the incidental powers authority granted federal credit unions by Congress. By overruling the determination of NCUA that share draft withdrawals are incidental to the business of credit unions, while providing no guidance as to what activities would be so allowed, the Court has left credit unions and their regulator in an impossible situation where the legality of other credit union functions may now be subject to question.

In view of the tremendous impact the Court's ruling has had on an entire industry and the statutory system devised by Congress to regulate it, CUNA and NAFCU respectfully urge that the Petition of the Solicitor General be granted.

While legislation currently pending in Congress would reverse the Court of Appeals decision and could render this litigation moot, the enactment of these proposals is hardly assured. For the reasons stated below, it is believed that the Court of Appeals seriously erred in construing existing law. That error should be rectified to prevent serious harm to the nation's financial institutions and the public they serve.

b. Historical Background

Federal credit unions are nonprofit, cooperative associations incorporated under the Federal Credit Union Act, 12 U.S.C. Secs. 1751, *et seq.* They are supervised and regulated by the Petitioner NCUA, an independent agency within the executive branch, which also insures credit union accounts through a deposit insurance fund established by 12 U.S.C. Sec. 1783.

Like banks and other depository institutions, federal credit unions are primarily engaged in the business of receiving deposits of money and making loans. Unlike other depository institutions, however, a credit union may not deal with the general public, but instead is restricted to providing services only for its own members, who must share a common bond of employment, association or residency. *See,* 12 U.S.C. Sec. 1759. As a true cooperative, a credit union is organized on a democratic basis, with each member having one vote in electing a board of directors and a credit committee,

which direct the credit union's business. 12 U.S.C. Secs. 1760, 1761b, 1761c. In essence, federal credit unions were created as nonprofit alternatives to commercial banks so that individuals could join together to obtain financial services on a cooperative basis. Their basic purpose is to receive the funds of their members on deposit and thereby serve their members as a source of inexpensive credit.

By tradition, credit union deposits are referred to as "shares," although they bear little resemblance to shares of stock in an ordinary corporation. Instead, a member's shares, like a deposit, may be withdrawn in cash at any time and may be paid either to the member directly or to any third party the member may specify. Pursuant to 12 U.S.C. Sec. 1763, funds in share accounts may receive interest (referred to as "dividends") at rates declared periodically by the board of directors.

While shares may be withdrawn whenever a member may request, the Federal Credit Union Act is completely silent as to the mechanics by which withdrawals may be made. No procedures are prescribed by statute, and none is prohibited. Instead, Congress has explicitly empowered each credit union to determine for itself the manner in which its share accounts are to be handled, subject only to regulation by the NCUA. *See,* 12 U.S.C. Sec. 1757(6).[1]

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[1] With respect to deposit withdrawals, Congress has put federal credit unions in the same legal posture as national banks, which also have statutory power to *receive* deposits (12 U.S.C. Sec. 24 Seventh) but which lack express authority to provide for any particular method of deposit withdrawal. Indeed, the original National Bank Act of 1864 did not mention withdrawals by check or even use the terms "check" or "checking account." Act of

Given that broad grant of power, and in the absence of any statutory restrictions, federal credit unions have traditionally employed a wide variety of procedures for the handling of withdrawals, including withdrawals for payment directly to third parties. Hence, a member can direct, in person, in writing or by telephone, that a withdrawal be sent directly to a creditor in payment of the member's obligations. Withdrawals can be obtained in the form of money orders or travelers cheques for payments to third parties. Members can preauthorize their credit union to pay recurring bills on their behalf directly out of their accounts. For a number of years, many credit unions have furnished their members with "loan draft" forms which can be filled in by members and drawn on their credit unions to obtain payment of loan advances directly to third party payees to whom the drafts have been negotiated.

The legality of these various procedures is not disputed. It is also undisputed that because of their availability, credit union accounts have been traditionally used, not only for long-term savings, but also for day-to-day transactions and third-party payments.

By the early 1970's, developments in financial technologies had made it possible for credit unions to consider new procedures for handling their traditional

June 3, 1864, ch. 106, 13 Stat. 99. While various references to checks and checking have entered the national bank laws over the intervening years, these provisions merely regulate but do not explicitly authorize bank checking. *C.f.*, 12 U.S.C. Secs. 36(f), 92a(d). The national banking statutes make no reference at all to a number of other procedures which bank depositors may employ to withdraw their funds.

business of providing third-party payment services to those members that desired them. For the first time, credit unions in significant numbers were acquiring access to low-cost electronic data processing, so that more automated methods for share withdrawal could be handled economically. At the same time, increasing competition for short-term consumer dollars made it necessary for credit unions to become even more responsive to those members who wanted to use their shares for current transactions.

In response to these factors, the first share draft programs were put into operation in the fall of 1974.

NCUA had given the program its prior regulatory approval, concluding that credits unions could honor share withdrawal drafts as an exercise of their statutory incidental powers under 12 U.S.C. Sec. 1757(15).[2] At common law, and under the Uniform Commercial Code, a draft is nothing more than a written order by which one person (the drawer) directs another person from whom money is owed (the drawee) to discharge its obligation by paying funds to a third party (the payee) whom the drawee has specified. Uniform Com-

[2] Section 1757(15) provides that a federal credit union shall have the power "to exercise such incidental powers as shall be necessary or requisite to enable it to carry on effectively the business for which it is incorporated." Under established principles developed in cases construing the very similar grant of incidental powers to national banks, this language has the effect of authorizing federal credit unions to conduct any activity that is "convenient or useful" in connection with the performance of their established, statutory activities. *Arnold Tours* v. *Camp*, 472 F.2d 427, 432 (1st Cir., 1972); *M & M Leasing Corp.* v. *Seattle First Nat. Bank*, 563 F.2d 1377 (9th Cir., 1977), *cert. denied*, 98 S.Ct. 3069 (1978).

mercial Code, Sec. 3-104.[3] Since anyone can draw a draft by simply framing a written direction for the payment of money according to the form prescribed by law, NCUA concluded that there was no legal impediment to a member requesting a share withdrawal by drawing a draft against his or her credit union. At the same time, NCUA determined that in the absence of any prohibition there was no legal reason to prevent a credit union from paying a withdrawal request in the form of a draft, just as credit unions have always been permitted to honor other written orders and authorizations directing payment of withdrawals to third parties.

From an operational standpoint, a share draft takes the form of a sight draft drawn by the member on the credit union and "payable through" a commercial bank named on the instrument. That draft can be filled in by the member and negotiated to a merchant or other payee for cash or to obtain goods or services. The payee deposits the draft with a bank or other financial institution which, in turn, can send the draft through the banking system to the "payable through" bank for presentment to the credit union.

The development of share draft programs depended upon the availability of low-cost credit union data processing so that the clearing and payment of share drafts could be handled on an automated, cost-effective basis. Through a process referred to as "truncation," share drafts received by the payable-through bank are con-

[3] Citation is to the Uniform Commercial Code (1972 Official Text). Articles 3 and 4 of the U.C.C. deal with drafts, checks and other commercial paper and have been enacted in substantially identical form in all fifty states and the District of Columbia.

verted to an electronic medium and transmitted by computer to the processing center that handles the credit union's accounting. Upon presentment of the draft through this electronic procedure, funds are withdrawn from the member's share account (if the balance is sufficient), and the instrument is paid by the credit union.

Operational aspects of the initial share draft programs were originally approved on a pilot basis by NCUA pursuant to 12 C.F.R. Sec. 721.3, a regulation adopted by the agency to provide for experimental programs relating to electronic funds transfer and similar operational systems. On December 8, 1977, NCUA published a final rule, 12 C.F.R. Sec. 701.34, regulating the operation of share draft programs on a permanent basis. The validity of this rule was upheld by the District Court in *American Bankers Assoc.* v. *Connell,* 447 F.Supp. 296 (1978), reversed by the Court of Appeals below.

As of June 30, 1979, 878 federal credit unions had established operating share draft programs and had opened 997,992 individual and joint share accounts from which share draft withdrawals could be made. During the quarter ending that month, those credit unions paid 35 million, one hundred nine thousand three hundred fifty two drafts with an aggregate value of $2 billion, four hundred twenty six million, seven hundred ninety two thousand, three hundred three dollars.

The development of share drafts from a pilot program to a major financial service did not occur without Congressional knowledge and supervision. Between October, 1974, when the program began, and the end

of 1976, the House and Senate oversight committees on federal credit unions specifically reviewed the share draft program on numerous occasions. *See,* e.g., *Financial Institutions Act of 1975; Hearings Before the Subcomm. on Financial Institutions of the Senate Comm. on Banking, Housing and Urban Affairs,* 94th Cong., 1st Sess., at 13, 583, 602-608, 687-689 (1975); *Regulation Q: Hearings Before the Subcomm. on Financial Institutions of the House Comm. on Banking, Currency, and Housing,* 94th Cong., 1st Sess., at 2256, 2291 (1975); *Financial Institutions and the Nation's Economy: Hearings Before the Subcomm. on Financial Institutions of the House Comm. on Banking, Currency, and Housing,* 94th Cong., 1st and 2nd Sess., pt. 2, at 1182 (1975); *Financial Reform Act of 1976: Hearings Before the Subcomm. on Financial Institutions of the House Comm. on Banking, Currency and Housing,* 94th Cong., 2nd Sess., at 80-81 (1976). As early as May 16, 1975, NCUA's Administrator specifically advised Congress that he had concluded that no new legislation was necessary to permit the program to be established on a permanent basis. *Financial Institutions Act of 1975: Hearings Before the Subcomm. on Financial Institutions of the Senate Comm. on Banking, Housing and Urban Affairs,* 94th Cong., 1st Sess., at 608.

With this background, and in April, 1977, when nearly a quarter million consumers were already using share drafts, Congress enacted P.L. 95-22 which included the most comprehensive amendments to the Federal Credit Union Act since its original passage in 1934. Far from indicating any disapproval of the agency's action in establishing the share draft program, P.L. 95-22 specifically confirmed that the terms and

conditions governing share accounts are to be determined by each credit union's board of directors, subject to NCUA regulation. Amending 12 U.S.C. Sec. 1757 (6), which confers the power to receive withdrawable shares, P.L. 95-22 added language to provide that a federal credit union may receive payments on shares "subject to such terms, rates, and conditions as may be established by the board of directors, within limitations prescribed by the [NCUA] Administrator."

c. Reasons for Granting the Writ

Fundamentally, the Court of Appeals erred in its apparent assumption that it was constrained to decide this and the two companion cases so as to achieve the same result in all three. In so doing, the court failed to adequately confront the very different legal issues underlying the three cases, which each turn on the construction of quite different statutory provisions. Instead, the court was led to erroneous conclusions by its philosophical belief that Congress should reexamine the respective roles of credit unions, banks and other financial institutions and readdress matters already entrusted to the financial regulators by law.

The unfortunate irony in the court's approach was that, while professing to preserve Congressional authority, the court seriously undermined the comprehensive legal and administrative structure devised by Congress to regulate financial institutions. In adopting laws providing for credit unions, banks and savings and loan associations, Congress wisely refrained from enacting detailed specifications for their day-to-day operations. Instead, basic powers were granted in general terms, and a large measure of discretion to con-

form those powers to changing circumstances was delegated to the agencies who are petitioners herein.

That Congressional approach to financial institutions is particularly apparent in the statutory treatment of credit union accounts. Federal credit unions have been given a general authority to receive deposits, but the manner of withdrawal is nowhere specified by statute. Instead, the law explicitly provides that the terms and conditions for handling these accounts are to be determined by each credit union's board, subject only to NCUA regulation.[4]

The absence of any Congressional limitations on credit union withdrawals fundamentally distinguishes this case from the other two involved in the instant petition. In the case of bank automatic transfer services and S & L remote terminals, the court could at least point to particular statutes that arguably prohibit the activities in question. *See,* 12 U.S.C. Secs. 371a, 1828(g), 1832(a), 1464(b)(1). With respect to federal credit unions, on the other hand, no such prohibition exists.

It should not be inferred that CUNA and NAFCU agree that the other two cases were decided correctly.

[4] In this connection, it is important to note that Congress created NCUA as an independent agency in 1970 with the specific intent that it provide more flexible and innovative regulation for federal credit unions. The Senate Banking Committee report on the bill creating NCUA stated the agency's mission as follows:

> "The committee believes that it is necessary to provide for the establishment of an independent agency to supervise and regulate the activities of the Federal credit unions. The committee believes that such an agency would be able to be more responsive to the needs of credit unions and to provide more *flexible and innovative regulation.*" S. Rep. No. 91-158, 91st Cong., 1st Sess. 3 (1970). (Emphasis added.)

To the contrary, we believe the Court of Appeals erred in deciding those cases as it did. The point is, however, that when Congress has intended to prohibit particular withdrawals from the accounts of other institutions, it has clearly expressed that intention with specific legislation. Thus, whatever effect 12 U.S.C. Sec. 1464(b)(1) may have on S & L electronic terminals, it is abundantly clear that savings and loan accounts cannot be withdrawn by check. Similarly, 12 U.S.C. Sec. 1832(b) unquestionably prohibits banks, S & L's and mutual savings banks from permitting withdrawals by negotiable or transferable instruments directly from interest-bearing accounts. Credit unions are not included in either of these prohibitions.

The Court of Appeals held that express statutory authority is necessary in order for an institution to permit withdrawals by negotiable draft. Congress apparently felt otherwise or it would have seen no reason to enact the prohibitions referred to above. Indeed, the great weight of judicial authority supports the proposition that no specific grant of authority is required to permit credit unions, savings and loans and other non-bank, financial institutions to provide for withdrawals by negotiable draft where the laws contain no prohibition. *Florida Bankers Assoc.* v. *Leon County Teachers Credit Union,* 359 So.2d 886 (Fla. 1st D.Ct. App. 1978). *cert. denied* and *appeal dismissed,* 368 So.2d 1366 (Fla. S.Ct. 1979) (credit union share drafts); *Wisconsin Bankers Assoc.* v. *Mutual Savings & Loan Assoc.,* 87 Wis.2d 470, 275 N.W.2d 130 (Wis. Ct.App., 1978) (S&L withdrawal drafts); *Washington Bankers Assoc.* v. *Washington Mutual Savings Bank,* —— Wash.2d ——, —— P.2d —— (Case No. 45875, August 2, 1979) (savings bank withdrawal drafts);

Consumers Savings Bank v. *Commissioner of Banks,* 361 Mass. 717, 282 N.E.2d 416 (Mass. 1972) (savings bank NOW drafts); *Savings Bank of Baltimore* v. *Bank Commissioner,* 248 Md. 461, 237 A.2d 45 (1968) (savings bank checking accounts); *Pennsylvania Bankers Assoc.* v. *Secretary of Banking,* 392 A.2d 1319 (Pa. S.Ct. 1978) (savings bank withdrawal drafts); *State* v. *Crookston Trust Co.,* 203 Minn. 512, 282 N.W. 138 (1938) (trust company checking); *State* v. *Lincoln Trust Co.,* 144 Mo. 562, 46 S.W. 593 (1898) (trust company checking).[5]

Accordingly, the Court of Appeals' conclusion that share drafts are "the practical equivalent of checks" does not dispose of the inquiry, as the court apparently believed. No statute reserves to banks any exclusive

[5] Only three reported cases, all of them distinguishable, have reached a contrary conclusion. In *New York State Bankers Assoc.* v. *Albright,* 38 N.Y.2d 430, 343 N.E.2d 735, 381 N.Y.S.2d 17 (1975) the court held that an amendment which simply removed a requirement that savings bank depositors present a passbook upon each withdrawal did not authorize withdrawals by negotiable draft where the law had been consistently interpreted to preclude draft withdrawals prior to the amendment. Similarly, in *Androscoggin County Savings Bank* v. *Cambell,* 282 A.2d 858 (Maine 1971), the court relied on a 1917 opinion of the state attorney general, consistently followed ever since, concluding that savings banks in that state could not offer checking accounts. As in the New York case, there was no indication that Maine savings banks had ever provided any third-party payment services whatever. Indeed, the Maine Supreme Court found as a fact that savings bank accounts had been traditionally reserved for long-term savings only. *Iowa Credit Union League* v. *Iowa Department of Banking,* 268 N.W.2d 165 (Iowa, 1978), holding against draft withdrawals from Iowa state-chartered credit unions, is distinguishable on the same basis. Iowa statutes expressly limit a state-chartered credit union to receiving the "*savings* of its members." No such limitation is to be found in the Federal Credit Union Act.

monopoly on the withdrawal of funds by check-like instruments. No statute expressly or by inference prohibits such withdrawals from credit unions.

CONCLUSION

For the foregoing reasons, we respectfully suggest that the Court of Appeals erred seriously in deciding that the use of credit union share drafts violates federal law. Moreover, the impact of its decision in this and the two companion cases will have a substantial and damaging impact on the nation's financial institutions and the millions of consumers who are using the services in question.

Because the Court of Appeals decided the three cases for the whole country, no conflict among the circuits will arise. Given the great importance of these cases, therefore, we respectfully urge this Honorable Court to grant the Petition.

Respectfully submitted,

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September 1979

Certificate of Service

I HEREBY CERTIFY that three copies of this document were mailed, postage prepaid, in accordance with the provisions of Rules 33.1 and 33.2(a) of the Rules of the United States Supreme Court, to each of the individuals listed below this 7th day of September, 1979.

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